Supreme Court, U.S.
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No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY and KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K. W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A," A. T. DAVIS, A. T. DAVIS TRUST "A," KAY DAVIS, KAY DAVIS TRUST "A," TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A. T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T. C. DAVIS, II, T. C. DAVIS, II TRUST, T. C. DAVIS, II TRUST "A," T. C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A," BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T. C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC. AND LOFFLAND BROTHERS COMPANY, KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

RESPONDENT KENDAVIS HOLDING COMPANY'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether a judge is disqualified under 28 U.S.C. § 455(b)(4) despite his lack of knowledge that he owns a financial interest in the corporate parent of a party to the proceeding.

2. Whether 28 U.S.C. § 455(c) creates a conclusive presumption that a judge knows everything about his or her financial and fiduciary interests that is revealed in materials in the judge's possession.

3. Whether the general rule that judges who learn of a disqualifying interest are required only to recuse themselves from future proceedings should be abandoned in favor of a rule that all orders entered by a disqualified judge are void, even in the absence of any showing of actual bias or impartiality.

4. Whether an appeal of the denial of motions to vacate the entered orders of a bankruptcy judge who later recused himself is rendered moot by the substantially complete implementation of those prior orders.

PARTIES TO THE PROCEEDING BELOW

In addition to the parties named in the caption of this case, the following were made parties to the proceeding in the Fifth Circuit:

The Bank of New York
The Chase Manhattan Bank, N.A.
Credit Commercial De France, New York Branch
Cummins Sales & Service, Inc.
Den Norske Creditbank
Development Bank of Singapore Limited
First City National Bank of Fort Worth
First City National Bank of Houston
First Interstate Bank of California
First National Bank & Trust Company of Oklahoma City (now known as Consolidated Asset Management as Administrator for Federal Deposit Insurance Corporation, in its corporate capacity)
First National Bank of Fort Worth
First RepublicBank Dallas, N.A.
First RepublicBank Fort Worth, N.A.
Frigette Corporation
Geodril, Inc.
Globe Machinery and Supply Company
Harrisburg, Inc.
InterFirst Bank Fort Worth, N.A.
Irving Trust Company
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers Eastern Hemisphere, Inc.
Loffland Brothers (Singapore) Pte., Ltd.
Mechanical Rubber Products Corporation
Miami-Dickerson Steel Company
Midco Equipment Co.
Mid-Continent Supply Co.
Moore & Sons, Inc.
Morgan Guaranty Trust Company of New York
The National Commercial Bank of Saudi Arabia
Nippon Kokan Kabushiki Kaisha
Rig-A-Lite Company, Inc.
Security Pacific National Bank
Sligo, Inc.
State Pipe & Supply Co.
Texas American Bank (Fort Worth), N.A.
Unit Rig & Equipment Co.

All of these companies are either banks that were members of the Official Unsecured Creditors' Committees or corporate affiliates of Kendavis Holding Company. Kendavis Holding Company has no corporate parent. Its affiliates, other than wholly-owned subsidiaries and the affiliates listed above, are:

CS&S Liquidating Co.
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers (Malaysia) Sdn. Bhd.
Mid-Continent Supply Co.
Nadrico Saudi Limited
State Pipe and Supply Co.
Stratoflex, Inc.
Unit Rig & Equipment Co.
Loffland Brothers de Venezuela, C.A.
Cumvenca, C.A.
Cummins Sales & Service de Venezuela, C.A.
KECO Limited

Upon the request of its clerk, the United States Court of Appeals for the Fifth Circuit was provided with a list of all pre-petition creditors in the various Kendavis cases. The list identified approximately 10,835 individuals and entities. If this Court so desires, copies of this list can be prepared and forwarded to the Court.

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RESPONDENT KENDAVIS HOLDING COMPANY'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The *per curiam* opinion of the United States Court of Appeals for the Fifth Circuit is unreported and is reprinted in the appendix to the petition at p. 6 ("Pet. App. 6"). The Memorandum Order of the United States District Court for Northern District of Texas, Dallas Division, is unpublished and is reprinted at Pet. App. 11.

JURISDICTION

Petitioners have applied for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit. There is no jurisdiction in this case because petitioners lack standing to assert their claims, and the unavailability of any effective relief renders petitioners' claims moot thereby negating the existence of a case or controversy justiciable under Article III of the Constitution. *See* U.S. Const., Art. III, § 2, cl. 1.

RELEVANT CONSTITUTIONAL AND STATUTORY PROVISIONS

United States Const., Article III, Section 2, Clause 1:

The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority, — to all Cases affecting Ambassadors, other public Ministers and Consuls; — to all Cases of admiralty and maritime Jurisdiction; — to Controversies to which the United States shall be a Party; — to Controversies between two or more States; — between a State and Citizens of another State; — between citizens of different States, — between citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.

United States Const., Amend. V:

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

28 U.S.C. § 455 (1982):

(a) Any justice, judge, or magistrate of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

(b) He shall also disqualify himself in the following circumstances:

(1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

(2) Where in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it;

(3) Where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy;

(4) He knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding;

(5) He or his spouse, or a person within the third degree of relationship to either of them, or the spouse of such a person:

(i) Is a party to the proceeding, or an officer, director, or trustee of a party;

(ii) Is acting as a lawyer in the proceeding;

(iii) Is known by the judge to have an interest that could be substantially affected by the outcome of the proceeding;

(iv) Is to the judge's knowledge likely to be a material witness in the proceeding.

(c) A judge should inform himself about his personal and fiduciary financial interests, and make a reasonable effort to inform himself about the personal financial interests of his spouse and minor children residing in his household.

(d) For the purposes of this section the following words or phrases shall have the meaning indicated:

(1) "proceeding" includes pretrial, trial, appellate review, or other stages of litigation;

(2) the degree of relationship is calculated according to the civil law system;

(3) "fiduciary" includes such relationships as executor, administrator, trustee, and guardian;

(4) "financial interest" means ownership of a legal or equitable interest, however small, or a relationship as a director, adviser, or other active participant in the affairs of a party, except that:

(i) Ownership in a mutual or common investment fund that holds securities is not a "financial interest" in such securities unless the judge participates in the management of the fund;

(ii) An office in an educational, religious, charitable, fraternal, or civic organization is not a "financial interest" in securities held by the organization;

(iii) The proprietary interest of a policyholder in a mutual insurance company, of a depositor in a mutual savings association, or a similar proprietary interest, is a "financial interest" in the organization only if the outcome of the proceeding could substantially affect the value of the interest;

(iv) Ownership of government securities is a "financial interest" in the issuer only if the outcome of the proceeding could substantially affect the value of the securities.

(e) No justice, judge, or magistrate shall accept from the parties to the proceeding a waiver of any ground for disqualification enumerated in subsection (b). Where the ground for disqualification arises only under subsection (a), waiver may be accepted provided it is preceded by a full disclosure on the record of the basis for disqualification.

STATEMENT OF THE CASE

Petitioners are either members of the family of the late Kenneth W. Davis, Sr. or are trusts, foundations or estates affiliated with the Davis family. Prior to April 16, 1987, Petitioners ("the Davis Family") held all outstanding shares of stock of respondent Kendavis Holding Company ("KHC"), which in turn owned all of the outstanding stock of Kendavis Industries International, Inc. ("KIII").

Certain creditors of KHC and KIII filed involuntary petitions for relief under chapter 11 of title 11 of the United States Code ("the Bankruptcy Code") against KHC and KIII on February 21, 1985. KHC and KIII consented to the entry of orders for relief, which United States Bankruptcy Judge Robert C. McGuire entered on March 19, 1985.

On November 24, 1986, after over 20 months of proceedings during which hundreds of orders were entered, Judge McGuire entered an order confirming a plan of reorganization for KHC and KIII ("the Confirmation Order"). Among other things, the confirmed plan provided that upon its effective date, KIII would be merged into KHC, the previously outstanding shares of stock of KHC would be cancelled, and new shares would be issued to holders of allowed Class 7 claims.

On the same day Judge McGuire entered the Confirmation Order, respondent KHC and certain of its subsidiaries, which were then under the control of the Davis Family,[1] filed an appeal of the Confirmation Order with the United States District Court for the Northern District of Texas, Dallas Division. The Davis Family appealed the Confirmation Order on December 4, 1986.

The District Court, in a series of orders entered on March 26, 1987, dismissed the appeals of the Confirmation Order filed by the Davis Family and the KHC entities, ruling that KHC and KIII's insolvency denied standing to KHC, KIII and the

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[1] Petitioner K. W. Davis, Jr. was then Chairman of the Board and President of KHC; T. Cullen Davis was Vice President of KHC; and petitioner Kay Davis was Secretary of KHC.

Davis Family as shareholders.[2] The District Court also denied the appellants' motions for a stay of implementation of the confirmed plan. R. App. 9, 11. The KHC entities and the Davis Family appealed to the United States Court of Appeals for the Fifth Circuit. On April 9 and April 10, the KHC entities filed motions seeking an expedited appeal of the Confirmation Order and a stay of implementation of the confirmed plan pending appeal.

On March 23, 1987, Bankruptcy Judge McGuire held a telephone conference with former counsel for respondent KHC and counsel for the Official Unsecured Creditors' Committees for KHC and KIII, during which Judge McGuire informed counsel that he had discovered the previous evening that a company in which he owned stock (J.P. Morgan Company, Inc.) was the owner of Morgan Guaranty Trust Company of New York, one of the bank creditors of KHC and KIII. See Pet. App. 18-21. Judge McGuire advised counsel that he had previously investigated the possible relationship of the two companies by making inquiry to his broker, and had been told they were unrelated. Judge McGuire explained that he had learned of the relationship when reviewing *The Value Line Investment Survey*, a quarterly investment report. Although Judge McGuire scheduled a status conference for March 26, 1987 to address procedures by which the disqualification issues might be resolved, the status conference was never held. Judge McGuire instead voluntarily recused himself on March 26, 1987.

On March 31, 1987, based on Judge McGuire's recusal, the Davis Family and the KHC entities filed motions with the District Court to vacate certain of Judge McGuire's orders, including the Confirmation Order. The District Court denied the motions to vacate on April 10, 1987 on the basis that Judge

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[2] The District Court's orders are reprinted in the Joint Appendix to Briefs in Opposition of Respondents Kendavis Holding Company and the Official Unsecured Creditors' Committees at pp. 1-11 ("R. App. 1-11").

McGuire's previous rulings should stand because he was not disqualified under either Section 455(a) or (b) until he discovered the relationship between J. P. Morgan & Sons and Morgan Guaranty. Pet. App. 11-17.

Upon the District Court's denial of the motions to vacate, the Davis Family and the KHC entities filed additional motions with the Fifth Circuit seeking an emergency stay of the effective date of the confirmed plan. The Fifth Circuit denied all motions for a stay by order of April 15, 1987; the Fifth Circuit, however, granted the motions for an expedited appeal.

As a result of the denials of any stay, the confirmed plan became effective on April 16, 1987. The Davis Family's stock was cancelled, KIII was merged into KHC, and KHC came under the control of new management. Since April 16, KHC has implemented the confirmed plan. Among other events, involuntary petitions for relief pending against twelve of KHC's subsidiaries were dismissed.[3]

Also, the KHC entities that, under former management, had appealed the Confirmation Order, retained new counsel and sought to dismiss the appeals pending before the Fifth Circuit as not in the best interests of the companies. KHC's former counsel, however, sought to continue to prosecute the appeal without authority from KHC. The Fifth Circuit permitted KHC's former counsel to participate in the appeal and to argue on behalf of KHC's former management.[4] The Fifth Circuit rendered the decision that is the subject of the Davis Family's petition on September 24, 1987.

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[3] Some of the more important actions taken to implement the confirmed plan are set forth in the Amended Affidavit of David E. Hawthorne, which was filed with the Fifth Circuit and which is reprinted at R. App. 12-24.

[4] The reference in the Fifth Circuit's opinion that "former management . . . claim[ed] rights of representation of creditors that can now be fully paid" refers to the argument of KHC's former counsel that, by virtue of their prior representation of KHC and KIII as debtors in possession, the Bankruptcy Code made them trustees for KHC and KIII's creditors.

SUMMARY OF THE ARGUMENT

Certiorari is unwarranted because the Fifth Circuit and the District Court properly applied 28 U.S.C. § 455(a) and (b) in holding that, under the circumstances, Bankruptcy Judge McGuire was not disqualified until he knew that he held a financial interest in the corporate parent of a party. The Davis Family attempts to avoid the assessment of particular facts properly made by the courts below by arguing that 28 U.S.C. § 455(c) creates a conclusive presumption of knowledge. Such a rule has never been accepted by any court, is unsupported by the statute and the legislative history, and would do violence to Congress' intent to fashion a practical solution to the practical problems of judicial disqualifications.

In addition, dismissal of the petition is appropriate. The implementation of the confirmed plan has rendered the Davis Family's appeal moot, and the Davis Family, as the former shareholders of an admittedly insolvent corporation, lack standing to assert their claims.

REASONS THE WRIT SHOULD NOT BE GRANTED

The Davis Family seeks this Court's review of a decision that the Fifth Circuit decided to render *per curiam* and unpublished because it had no precedential value and merely decided a particular case on the basis of well-settled principles of law. Pet. App. 6. Indeed, insofar as 28 U.S.C. § 455 is concerned, the Fifth Circuit opinion simply affirmed two factual findings by the District Court: one, a finding that Judge McGuire did not have actual knowledge of a financial interest; and two, a finding that a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual knowledge of his financial interest. Pet. App. 7, 14-15. As a result of the first finding, the district court concluded that Section 455(b) had not been violated. As a result of both findings, the district court concluded that Section 455(a) was not violated.

Stripped of its rhetoric, the Davis Family's petition is nothing more than an attempt to overturn the District Court's second finding by construing Section 455(b) in such a way as to eliminate the word "know" from the statute.[5] Interestingly, the Davis Family's argument begins with the admission that the District Court's first finding is correct — the judge did not have actual knowledge of an interest. "The bankruptcy judge . . . failed to recognize that substantially the entire business of J.P. Morgan was the ownership of Morgan Guaranty." Petition, p. 5. The Davis Family then argues that since the judge possessed information revealing the relationship, he should have known of the relationship, and since he should have known, "he must be concluded to have known . . .." Petition, p. 5.

The Davis Family can blind themselves to reality in this way only by resort to the procedural device of a conclusive presumption. Thus, the Davis Family urges that Section 455(b)(4) and Section 455(c), read together, "establish a standard by which a judge is charged, *conclusively*, with knowledge of that which information in his possession reveals about his financial interest . . .." Petition p. 15 (emphasis supplied). No court has accepted this proposition. One district court has expressly rejected it. *NEC Corp. v. Intel Corp.*, 654 F. Supp. 1256, 1257-58 (N.D. Cal.), *appeal docketed*, No. 87-7126 (9th Cir.) (March 30, 1987). Two circuit courts, in addition to the Fifth Circuit, have implicitly rejected the

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[5] Although the petition does not identify Section 455(a) in the Questions Presented, the Davis Family does suggest that the Fifth Circuit abandoned its construction of Section 455(a) in *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986), *cert. granted*, ___ U.S. ___, 107 S. Ct. 1368 (1987) (No. 86-957) (argued December 9, 1987). Petition, pp. 6-7. This suggestion is curious in light of the District Court's express conclusion that "a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual or constructive knowledge of any conflict," Pet. App. 15-16, and the Fifth Circuit's conclusion that "we think it clear that the bankruptcy judge's impartiality could not be reasonably questioned." Pet. App. 7. No departure from the *Health Services* test is apparent — only a different conclusion based on different facts.

proposition. *See Davis v. Xerox*, 811 F.2d 1293, 1296 (9th Cir. 1986), *cert. denied*, ___ U.S. ___, 56 U.S.L.W. 3383 (Nov. 30, 1987) ("We are unwilling to presume that because the judge once knew, he could not have forgotten"); *Hodosh v. Block Drug Co.*, 790 F.2d 880 (Fed. Cir.), *cert. denied*, ___ U.S. ___, 107 S. Ct. 106 (1986) (no basis for disqualification where judge did not know that a company in which his spouse owned stock acquired a party to the proceeding); *Union Carbide Corp. v. U.S. Cutting Service, Inc.*, 782 F.2d 710, 713-15 (7th Cir. 1986) (judge permitted to continue to sit in class action case when, after discovering that two companies in which her spouse held stock were unnamed class members, she had her spouse dispose of the stock).

Yet the existence of a conclusive presumption of knowledge is central to the Davis Family's petition; without it, they are left with the facts that even they admit — Judge McGuire did not know of the relationship between J. P. Morgan and Morgan Guaranty, Petition, p. 5, and his "actual, subjective integrity is not called into question." Petition, p. 18. Recognizing the importance to their position of a conclusive presumption, the Davis Family argues that "[a]ny other position vitiates § 455(b)(4)." *Id.* To the contrary, adoption of a conclusive presumption is precisely what Congress sought to avoid when it rejected a version of the financial interest subsection of Section 455 that did not include a knowledge test in favor of the present statute, which does include a knowledge test.

In Enacting 28 U.S.C. § 455, Congress Sought a Practical Solution to Practical Problems

Unable to cite any judicial precedent for their proposition, the Davis Family selectively refers to the legislative history of Section 455 to suggest that the overwhelming concern of Congress in enacting Section 455 was to foster public confidence by avoiding the appearance of impropriety. Aside from the fact that public confidence in the judiciary and the appear-

ance of propriety are both promoted by Judge McGuire's courage in coming forward and voluntarily recusing himself as soon as he learned of his financial interest, the Davis Family has ignored an equal, if not greater concern of Congress — the dilemma faced by every judge who had tried to find guidance for his conduct in the vague statute that preceded the current one. The former version of Section 455 provided:

> Any justice or judge of the United States shall disqualify himself in any case in which he has a substantial interest, has been of counsel, is or has been a material witness, or is so related to or connected with any party or his attorney as to render it improper, in his opinion, for him to sit on the trial, appeal or other proceeding therein.

Act of June 25, 1948, c. 646, § 1, 62 Stat. 908 (1948) (current version at 28 U.S.C. § 455 (1982)).

The Congressional hearings and reports make repeated reference to Congress' desire to replace the uncertain test of the former statute with a clear and certain standard for judges. *E.g.*, H. Rep. No. 93-1453, 93d Cong. 2d Sess. (1974), reprinted in 1974 U.S. Code Cong. and Admin. News 6351 ("House Report") at 6352, 6355; *Judicial Disqualification: Hearing on S. 1064 Before the Subcommittee on Improvements in Judicial Machinery of the Committee on the Judiciary, United States Senate*, 93d Cong. 1st Sess. 24 (1973) ("Senate Hearings") (hearings were held in the Senate on both July 14, 1971 and May 17, 1973, and were reported in the single volume cited above). For example, Senator Burdick opened both the 1971 and 1973 Senate hearings by noting that the legal standard created by the then-existing statute had the effect of "placing a judge on the horns of a dilemma." Senate Hearings at 2, 74.[6] The uncertainty of the rule that a judge was disqualified only

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[6] The current version of Section 455 is the result of Congressional hearings in 1971 and 1973, during which Congress considered three different bills on judicial disqualification. S. 1553 was introduced by Senator Hollings, and S. 1886 was introduced by Senator Bayh, both in 1971. In 1973, the bill before the Senate, S. 1064, was introduced by Senator Burdick and was based on the newly adopted ABA Code of Judicial Conduct.

for a "substantial interest," coupled with the existing case law that the judge had a "duty to sit" unless disqualified, *e.g.*, *Edwards v. United States*, 334 F.2d 360, 362 n.2 (5th Cir. 1964), *cert. denied*, 379 U.S. 1000 (1965), left many judges to act at their own peril.

Indeed, as the Davis Family notes, Petition, pp. 8-9, the new legislation was inspired in part by the controversy surrounding the nomination of Judge Haynsworth to this Court. Senator Hollings first tried to amend the disqualification statute during the Haynsworth hearings, when he saw the inequitable position into which Judge Haynsworth had been forced by the vague "substantial interest" and "in his opinion" standards. Senate Hearings at 24. Although the American Bar Association cleared Judge Haynsworth of any misconduct for failing to disqualify himself in certain cases on the basis of financial interest, many considered the resulting "cloud of doubt" to be unfair to the judge. Senate Hearings at 24. Section 455 was designed to eliminate the uncertainty. As Senator Burdick noted at the 1973 hearings:

> It is believed that the enactment of this bill will do much to remove our Federal judges from the horns of the dilemma they currently face. Congress will have specified the amount and type of financial interest, the degree of relationship, and the prior association which forces disqualification. Congress will have relieved the Judge of the "duty-to-sit" which presently clouds his judgment when he is forced to determine whether his interest is a case so "substantial" as to require his disqualification.

Senate Hearings at 74.

Given Congress' concern that judges needed a clear, workable standard for determining when they were disqualified, the legislative history reflects that the concept of Section 455 was to promote the appearance of impartiality not by imposing draconian punishments for failing to abide by impossible standards, but by establishing standards that judges

could readily implement. In the 1971 Senate hearings, Professor John P. Frank stated that "[t]he goal is to get to something which is practical enough to be livable." Senate Hearings at 37. Senator Hollings described his bill as "a comprehensive but practical approach to judicial disqualification." Senate Hearings at 24. The final statute explicitly deals with the Congressional concern over one particular practical problem — the impossibility of keeping track of the holdings of a mutual fund — by exempting mutual funds from the general rule. 28 U.S.C. § 455(d)(4)(i) (1982). Similarly, the knowledge requirement of Section 455(b)(4) stems from Congressional recognition that a workable standard must be consistent with the practical problems of everyday compliance.

The knowledge requirement of Section 455(b)(4) was deliberately added in light of express recognition by the Senate of the practical problems that would result if knowledge were not required. Senator Bayh's bill differed from the other bills and the statute ultimately adopted in that it required a judge to disqualify himself "in any case in which he has an interest," rather than when he *knows* that he has a financial interest. *Compare* S. 1886, Senate Hearings at 6 (the Bayh bill) *with* S. 1553, Senate Hearings at 3 (the Hollings bill) *and* S. 1064, Senate Hearings at 130 (the Burdick bill). *See also* 28 U.S.C. § 455(b)(4) (1982).

The practical problems with the Bayh bill came to light during the Senator's testimony:

> Senator GURNEY: . . . I think it might be difficult, perhaps, sometimes for a judge to keep track, possibly, of the holdings of a major corporation in subsidiaries, and he might have known them at the time he acquired his stock but there might be changes made later on. Suppose he ran afoul of this particular provision in your bill unwittingly and unknowingly, what happens if he goes ahead and tries the case?
>
> Senator BAYH: Well, I think that case would then be subject to reversal on appeal.

> Senator GURNEY: Well, suppose it were not discovered until the case was through; then what?
>
> Senator BAYH: Then, it would have to be considered on its merits at the time. You have to consider each case on its merits.
>
> * * *
>
> Senator GURNEY: My question is directed as to what is going to happen to the litigation in cases and the respective rights of the parties if the case is tried and unwittingly falls within this rule?
>
> If we are going to pass a bill here, *we had better make darn sure that we have got a bill that is not going to cause all kinds of problems down the road.*

Senate Hearings, at 17, 18 (emphasis supplied). Senators Burdick and Gurney then commented on the practical benefits of the knowledge requirement in the ABA Code of Judicial Conduct:

> Senator BURDICK: I wonder if the answer might lie in the ABA's suggestion that they base this interest in subsidiaries on knowledge, the judge, if he knew? If he knows that he individually, or his fiduciary, or other member of his immediate family, or any member of his family residing in the household has a financial interest, if he knows of the interest, it is based upon knowledge.
>
> * * *
>
> Senator GURNEY: . . . I think a judge could own something in Western, which is one of the conglomerates and they are buying and selling all of the time, and he could fall afoul of that not really knowing what he owned at any one time, as far as a subsidiary is concerned. So, what I am saying, is I think we have a real problem here. We are going to have a problem.

Senate Hearings at 38.[7] The point was raised again with Professor Frank, who helped draft the Bayh bill:

> MR. FRANK: [W]e also have to keep in mind the point Senator Gurney made in the colloquy with Senator Bayh, and that is we do not want to clog judicial administration by having mistakes turn up later that require retrials or anything of that sort. And there is a limit to what the judge can do.

Senate Hearings at 36. Thus Congress, in adopting the Burdick bill recognized the significance of the knowledge requirement found in Section 455(b)(4), yet the Davis Family would have this Court read that requirement out of the law by adopting a position that has never before been accepted by any court — that the combination of Section 455(b)(4) and Section 455(c) creates a conclusive presumption of knowledge.

There is no basis in the legislative history for such a reading. Nor does such a reading create the "objective test" that the Davis Family claims it does. Petition, p. 18. Conclusive presumptions are not "tests" at all; they are procedural devices that eliminate the need for fact-finding. The objective test instead asks what reasonable persons would conclude from the circumstances. *See, e.g., Boleman v. Congdon and Carpenter Co.*, 638 F.2d. 2, 4 (1st Cir. 1981) (In the context of formation of a contract, a binding offer is made when the offeror leads the offeree reasonably to believe one has been made). As the Ninth Circuit said:

> The right course under § 455(b) as under § 455(a) is to proceed on a case by case basis, determining the

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[7] The Davis Family notes that this Court has not ruled whether the ownership of the stock of the corporate parent of a party is ownership of a financial interest of a party. Petition, p. 7. Bankruptcy Judge McGuire best characterized this, however, as "a nonissue," Pet. App. 21, and it is not implicated by the petition. No one seriously contests that given that the overwhelming majority of J. P. Morgan's business is the ownership of the Morgan Guaranty Bank, once the relationship was discovered by the judge, disqualification was warranted under § 455(a) even if not under § 455(b)(4). While there might have been a question whether the parties could have agreed to let Judge McGuire dispose of his stock and continue in the case, *see* 28 U.S.C. § 455(e), Judge McGuire eliminated that potential issue by voluntarily recusing himself.

> existence of disqualifying knowledge at the time the judge sat, *in the way that a state of mind is normally determined, from inspection of all the circumstances.*

Davis v. Xerox, 811 F.2d at 1296 (emphasis supplied).

Nowhere does the legislative history suggest any Congressional intent to depart from this normal test for knowledge. Even the statement of Professor Frank quoted by the Davis Family — "they will not be excused from failing to know what they have" — does not unambiguously express an intent to depart from the normal objective test for determining knowledge. Petition, p. 15, citing Senate Hearings at 115.[8] In addition, Professor Frank's testimony helps to put his prepared statement in perspective. Even he acknowledged that "there is a limit to what the judge can do." Senate Hearings at 36. Also, in the discussion of the desirability of a knowledge standard, this exchange took place:

> Senator BURDICK: Why do we not follow the pure rule in regard to direct parent companies and apply the knowledge rule to the subsidiaries? Would that not take care of it?
>
> MR. FRANK: It would; and it might well be a good solution so long as at least you could not remove some duty on the part of the judge to be informed. In other words, you could not have a fellow *utterly neglecting* to find out.

Senate Hearings at 44. (emphasis supplied).

Section 455(c) does not create a conclusive presumption of knowledge. In fact, it says nothing about what a judge actually or presumably knows. Nor does it state a mandatory duty of the judge to ascertain everything possible about his holdings. It merely directs the judge that he "*should* inform himself," 28 U.S.C. § 455(c) (emphasis supplied), and precludes the use of

[8] The quoted remarks come not from Professor Frank's live testimony, but from his prepared statement, which was neither discussed nor explicitly adopted by any member of Congress.

a blind trust to avoid disqualification. *See NEC Corp.*, 654 F.Supp. at 1258 n.2.

Particularly in light of the Congressional debate on whether to adopt a knowledge requirement, meaning must be given to the different words Congress selected: "know," "shall" and "should." *See Reiter v. Sonotone Corp.*, 442 U.S. 330, 338-339 (1979) (in construing a statute, courts are obliged to give effect, if possible, to every word Congress used). Here subsections (b)(4), (b)(5)(iii) and (b)(5)(iv) of Section 455 require knowledge by the judge; the other subsections do not. Where Congress includes particular language in one section of a statute, but omits it in another section of the same act, it is generally presumed that Congress acted intentionally and purposely in so doing. *Russello v. United States*, 464 U.S. 16, 22-23 (1983). Comparing the various subsections of Section 455, Congress' intent and purpose becomes clear. Congress included a knowledge requirement whenever it perceived that an absolute rule would raise substantial practical difficulties. Similarly, Congress' selection of "should" in Section 455(c) instead of "shall" as in Sections 455(a) and (b) suggests that Congress intended to articulate mandatory duties in Sections 455(a) and (b), but not in Section 455(c).

The Davis Family simply seeks to blur the distinctions among the various subsections of Section 455, so as to read into one part of the statute useful language from another. This the Davis Family cannot do, for under accepted rules of statutory construction, each word must be given meaning, and clearly different words should not be given the same meaning.

Due Process Does Not Require the Interrogation Of Bankruptcy Judge McGuire

The Davis Family also suggests that the decision below conflicts with existing law requiring a due process hearing. Judge McGuire's prompt disclosure of his discovery of his interest, however, enabled the Davis Family to receive a due

process hearing. The District Court considered the Davis Family's arguments concerning Section 455 on their merits and rejected them. The Fifth Circuit considered an emergency motion for stay and denied it. Finally, the Fifth Circuit reviewed, and affirmed, the District Court's decision. The only conceivable question is whether the District Court erred in quashing the notice of Bankruptcy Judge McGuire's deposition.

Traditionally the trial court is given wide latitude in controlling the scope of discovery, and its decisions are reviewed under the abuse of discretion standard. *See, e.g., O'Neal v. Riceland Foods*, 684 F.2d 577 (8th Cir. 1982) (district court has wide discretion in its handling of discovery matters; its decisions are to be upheld unless, in the totality of the circumstances, its rulings constitute such a gross abuse of discretion as to result in fundamental unfairness). On review, the Fifth Circuit found no basis for questioning Bankruptcy Judge McGuire's statements in his judicial capacity. Pet. App. 7.

Unless due process is to require the unseemly interrogation under oath of every judge who, discovering information new to him, advises the parties and seeks to cure any potential disqualification problems, there is no call for certiorari here. The district court in *NEC Corp.*, rejecting arguments similar to those advanced here by the Davis Family,[9] recognized the significant problems of such an "inquisition into the judge's state of mind." As observed by the *NEC* court:

> This inquiry might entail deposing, examining, cross-examining, and impeaching the judge and might

[9] NEC Corporation and the Davis Family both filed *amicus curiae* briefs in *Liljeberg v. Health Services Acquisition Corp.*, (No. 86-957), argued December 9, 1987, urging the adoption of a conclusive presumption rule. See Brief of Amici Curiae Kenneth W. Davis, Jr., et al., *Liljeberg*, (No. 86-957), filed July 23, 1987; Brief of Amici Curiae NEC Corporation and NEC Electronics, Inc. in Support of Respondent Health Services Acquisition Corp., *Liljeberg*, (No. 86-957), filed July 22, 1987.

> require another judge to make findings of fact on a colleague's credibility. NEC is correct in arguing that this "unseemly procedure" . . . would do little to advance the statutory purpose to "promote public confidence in the impartiality of the judicial process," House Report, . . . at 1974 U.S. Code Cong. & Admin. News 6357, and should be avoided.

NEC Corp., 654 F.Supp. at 1258. In the instant case, Judge McGuire, by coming forward, and by recusing himself, has already best promoted public confidence in the impartiality of the judicial process.

Vacating Bankruptcy Judge McGuire's Orders Would Demean, Not Promote, The Image of the Federal Judiciary.

The practical effect of vacating Bankruptcy Judge McGuire's orders may well be the liquidation of Kendavis Holding Company, which recently emerged from over two years of bankruptcy proceedings during which Judge McGuire issued hundreds of orders and the estate paid over 20 million dollars in professional fees. R. App. 24. Given that prior to the implementation of the confirmed plan, KHC was insolvent, it is highly doubtful that the company could survive another journey through the bankruptcy process. Yet the relief sought would require just that — even the Orders for Relief were entered by Judge McGuire and, under the Davis Family's theory, would be vacated.

It is simply not plausible that the thousands of creditors and other persons affected by Judge McGuire's orders, or the public at large, would find any justice if the Davis Family were able, in the absence of any showing of actual bias or impartiality, to thwart the entire reorganization process. In the first place, the Davis Family, as shareholders of an admittedly insolvent corporation, lacked standing to challenge the Bankruptcy Court's orders on their merits. *See, e.g., In re Dutch Inn of Orlando, Ltd.*, 614 F.2d 506, 508 (5th Cir. 1980) (limited partners of insolvent limited partnership lacked standing). Second, the fact that some members of the Davis Family may

previously have been the principal officers and directors of KHC does not grant them any independent standing. *See, e.g., In re Johns-Manville Corp.*, 801 F.2d 60, 65 (2d Cir. 1986). Third, the substantive challenges to the confirmed plan that the Davis Family did assert were meritless. The Fifth Circuit found them to be "frivolous." Pet. App. 7.

From a broader perspective, much of the public's confidence and faith in the judiciary stems from the finality of judicial decisions. If the Davis Family's position were to be accepted, any creditor or other person dealing with an entity operating under the protection of the Bankruptcy Code would have to live with the fear that even the simplest, most benign, mistake by the judge could void every action taken during the course of the proceedings. Particularly when bankruptcies may involve thousands of creditors, the potential for innocent oversight is great, and the practical effect of the Davis Family's rule may be the wholesale recusal of all bankruptcy judges who own securities of individual corporations. "Such broad-scale disqualification is an unlikely purpose to impute to Congress in passing section 455(b)." *Union Carbide Corp.*, 782 F.2d at 715 (discussing the problems of unidentified corporate class members). Also, broad-scale disqualification and retrospective recusal are hardly the practical, easy-to-implement, solution sought by Congress in drafting Section 455. They are, instead, precisely what troubled Professor Frank when he testified that "we do not want to clog judicial administration by having mistakes turn up later that require retrials or anything like that." Senate Hearings at 36.

Judge McGuire's Orders Should Not Be Vacated Because The Appeal of the District Court's Denial of the Motions to Vacate Has Been Rendered Moot

Although the KHC entities, under former management, repeatedly sought a stay of the implementation of the confirmed plan, no stay was ever issued to bar the implementation of the plan on its Effective Date, April 16, 1987. Accordingly,

the confirmed plan became effective on April 16, 1987, and since that time, KHC (under its new management as provided for by the plan) has taken numerous steps to implement the confirmed plan. Many of these steps are detailed in the Amended Affidavit of David E. Hawthorne, which was filed with the Fifth Circuit.[10] As even the Davis Family conceded before the Fifth Circuit, the effect of these steps is the "substantial consummation" of the confirmed plan. *See* 11 U.S.C. § 1101(1) (1982).

Just as Congress was mindful when drafting 28 U.S.C. § 455 of the needs for finality of judicial decisions and efficient administration of the judicial system, so also was it mindful that absent a stay pending appeal, parties involved in a bankruptcy case must be able to rely upon the finality of a court's orders.[11]

The circuit courts are nearly unanimous in applying the mootness doctrine in the bankruptcy context to require dismissal of challenges to a confirmed plan of reorganization that has been so substantially implemented that effective judicial relief is no longer available to the appellant, even if the appeal were to be decided in its favor. *See, e.g., In re AOV Industries, Inc.*, 792 F.2d 1140 (D.C. Cir. 1986); *In re Sun Country Development, Inc.*, 764 F.2d 406 (5th Cir. 1985); *In re Information Dialogues, Inc.*, 662 F.2d 475 (8th Cir. 1981). Indeed, the practical needs in Chapter 11 proceedings for creditors, debtors and non-parties to rely on the finality of a debtor's court-approved actions are such that, as the Ninth Circuit stated in a pre-Code case, "reversal of [an] order confirming the plan of arrangement, which would knock the

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[10] The Amended Affidavit is reprinted at R. App. 12-24.

[11] This need was recognized by Congress in relation to sales of assets. Section 363(m) of the Bankruptcy Code provides that an order authorizing use, sale or lease of a debtor's property is final, even if the order has been reversed on appeal, unless the appellant obtains a stay pending the appeal. 11 U.S.C. § 363(m) (1982). Courts have applied the same analysis to appeals from orders confirming a plan of reorganization. *See generally* Broude, Reorganizations Under Chapter 11 of the Bankruptcy Code, § 14.01[1] (1986).

props out from under the authorization for every transaction that has taken place, would do nothing other than create an unmanageable, uncontrollable situation . . .." *In re Roberts Farms*, 652 F.2d 793, 797 (9th Cir. 1981).

Most recently, the Eleventh Circuit held that when a confirmed plan has been substantially consummated and all creditors either have been paid or have had sufficient monies reserved to pay their claims if allowed, an appeal of the confirmation of the plan is moot. *Miami Center Limited Partnership v. Bank of New York*, 820 F.2d 376 (11th Cir.), *modified on other grounds*, 826 F.2d 1010 (1987). This is precisely the case here. Virtually all required corporate actions have been taken, KHC has paid in full the holders of allowed Class 1 through 6 claims, and stock and notes have been issued to the holders of Class 7 claims. Only holders of Class 7 claims, who are now the shareholders of KHC, await receipt of cash distributions. R. App. 12-24. Since all classes have received payment or other distributions, vacating the Confirmation Order, and the hundreds of Judge McGuire's other orders, would serve no useful purpose. It would simply reinstate the former shareholders of acknowledged insolvent debtors, and wreak havoc upon the affairs of hundreds of creditors. Accordingly, the controversy is moot.

CONCLUSION

For the reasons stated above, this Court should dismiss or deny the petition for writ of certioriari.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Brett A. Ringle, counsel of record for Respondent Kendavis Holding Company and a member of the Bar of the Supreme Court of the United States, hereby certify that I have served three copies of Respondent Kendavis Holding Company's Brief in Opposition to Petition for Writ of Certiorari and the Joint Appendix to Briefs in Opposition of Respondents Kendavis Holding Company and the Official Unsecured Creditors' Committees on all parties required to be served, by depositing three copies of each in the United States mail, on this

20th day of December, 1987, with first class postage prepaid, addressed to the listed counsel of record at the addresses indicated.

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